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STATE AND LOCAL GOVERNMENT

I. INDUSTRIAL DEVELOPMENT IS A PUBLIC PURPOSE

Only three years after ruling that industrial development does not serve a public purpose, the South Carolina Supreme Court reversed itself in *Nichols v. South Carolina Research Authority*.[1] In *Nichols* the court expressly overruled that portion of *Byrd v. County of Florence*[2] which held that industrial development could not be a public purpose for which public revenues may be appropriated and expended. In changing its interpretation, the court adopted what appears to be the position of the majority of states which have considered the question.[3]

Nichols involved constitutional and statutory challenges to the validity of the act that created the South Carolina Research Authority.[4] The Authority was created to promote high technology industries and research in South Carolina. The Authority's primary function was to construct and operate research parks. The legislature gave the Authority 1500 acres of state-owned property and empowered the Authority to borrow money, issue revenue bonds, and transfer land.[5] The circuit court invalidated the act creating the Authority partially because of the ruling in *Byrd*.[6]

In concluding that *Byrd* had been wrongly decided, at least in its restriction of the scope of "public purpose," the South

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1. 290 S.C. 415, 351 S.E.2d 155 (1986). The court also reached the following other significant conclusions: The Authority is an agency of the state; mortgaging land held by the Authority would not constitute an impermissible pledge of the state's credit; the Authority may not legally enter into joint ventures with private firms; transfers of land to private enterprises at less than full market value by the Authority are not necessarily prohibited (if indirect benefits would accrue to the state); and the statute that gave the Authority the option of whether to comply with the Advanced Refunding Act is unconstitutional special legislation.

2. 281 S.C. 402, 315 S.E.2d 804 (1984).

3. *See infra* p. 163 & note 16.

4. *See* Act Effective April 29, 1983, 1983 S.C. Acts 50 *as amended by* Act Effective March 22, 1984, 1984 S.C. Acts 308 & Act Effective March 23, 1984, 1984 S.C. Acts 309; S.C. CODE ANN. § 13-17-10 to -170 (Law. Co-op. Supp. 1986).

5. 290 S.C. at 417, 351 S.E.2d at 156.

6. *Id.* at 423, 351 S.E.2d at 159.

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Carolina Supreme Court first noted that the scope of judicial review of legislative acts was limited. Legislative acts are to be presumed constitutional and not invalidated unless clearly repugnant to the constitution.[7]

The court then explained that "public purpose" is a fluid concept, changing in context with the needs of society.[8] The court cited authority from several jurisdictions, including Maryland, Wisconsin, Maine, and Missouri, to support its conclusion that industrial development serves a public purpose.[9] Emphasizing that "public purpose" is a legislative determination, the court listed many South Carolina cases upholding the constitutionality of public purpose determinations.[10]

The court reviewed the record in *Byrd* and noted especially the severe economic problems suffered in Florence County prior to *Byrd*. The ordinance at issue in *Byrd* was an attempt by the Florence County Council to encourage industrial development to alleviate these problems. The court then reviewed the many South Carolina cases which have addressed challenges to governmental spending on "public purposes" grounds. Admitting that the cases were not entirely consistent, the court nonetheless noted that they reflected a "trend toward broadening the coverage of what constitutes a valid public purpose."[11] Relying primarily on the 1978 case *Bauer v. South Carolina State Housing Authority*,[12] the court stated that public purpose is not destroyed because of the "mere fact that benefits will accrue to private individuals."[13] The opinion adopted the part of Chief Justice Ness' dissent in *Byrd* which pointed out the anomalous result of allowing the State Development Board to spend millions of dollars to attract industry to the state while denying a county the opportunity to use local funds for the same purposes.

Byrd was not, however, entirely overruled. The four point standard used in *Byrd* to test and reject a statute for financing industrial development was explicitly retained in *Nichols*.[14] De-

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7. *Id.* at 424, 351 S.E.2d at 160.
8. *Id.* at 425, 351 S.E.2d at 160.
9. *Id.* at 425-26, 351 S.E.2d at 161.
10. *Id.* at 426, 351 S.E.2d at 161.
11. *Id.* at 427-28, 351 S.E.2d at 162.
12. 271 S.C. 219, 246 S.E.2d 869 (1978).
13. 290 S.C. at 428, 351 S.E.2d at 162.
14. "The Court should *first* determine the ultimate goal or benefit to the public

spite the controversial holding of *Byrd*, it has been cited in only two reported cases[15] and not for its "industrial development" holding, but for the proposition that "public purpose" is a fluid concept to be decided according to the particular circumstances of each case.

Authorities as early as 1941 indicated a broadening of the scope of activities which may be classified as serving a "public purpose."[16] Substantial limits on state and local government efforts to aid or subsidize private enterprise, however, remained in place as much as thirty years later.[17] More recently, the courts have shown a greater willingness to find that projects promoting private industry serve a public purpose.[18] South Carolina has accepted the logical and dominant view of the scope of public purpose. Employment and general prosperity within an area are important to the community and its residents, and, therefore, the legislature has the authority to determine which projects support these needs and thereby serve a public purpose.

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intended by the project. *Second*, the Court should analyze whether public or private parties will be the primary beneficiaries. *Third*, the speculative nature of the project must be considered. *Fourth*, the Court must analyze and balance the probability that the public interest will be ultimately served and to what degree." *Id.* at 429, 351 S.E.2d at 163 (quoting 281 S.C. at 407, 315 S.E.2d at 806 (emphasis added)).

15. Wolper v. City Council of Charleston, 287 S.C. 209, 216, 336 S.E.2d 871, 875 (1985); South Carolina Pub. Serv. Auth. v. Summers, 282 S.C. 148, 151, 318 S.E.2d 113, 114 (1984).

16. 37 AM. JUR. *Municipal Corporations* § 132, at 746 (1941) (discussion of enterprises in which municipal corporations may themselves engage).

17. *See* 56 AM. JUR. 2D *Municipal Corporations* § 203 (1971); *see also* Annotation, *Constitutionality of Statute Authorizing State To Loan Money or Engage in Business of a Private Nature*, 115 A.L.R. 1459 (1938); Annotation, *Encouragement or Promotion of Industry Not in Nature of Public Utility, Carried on by Private Enterprise, as Public Purpose for Which Tax May Be Imposed or Public Money Appropriated*, 112 A.L.R. 571 (1938).

18. *See, e.g.*, People *ex. rel.* Salem v. McMackin, 53 Ill. 2d 347, 358, 291 N.E.2d 807, 813 (1972) (industrial project revenue bond serves public purpose of reducing unemployment); Hawley v. South Bend Dep't of Redev., 270 Ind. 109, 120, 383 N.E.2d 333, 341 (1978) (resale of land for private shopping mall after slum clearance held within realm of "public purpose"); Anderson v. O'Brien, 84 Wash. 2d 64, 70, 524 P.2d 390, 393-94 (1974) (reducing unemployment serves a public purpose). The court in *Nichols* recognized the trend toward broadening the definition of public purpose. *See* 290 S.C. at 425-26, 351 S.E.2d at 161. *See generally* 35 WORDS & PHRASES *Public Purpose* (Supp. 1987). Some courts have also held that urban redevelopment by private enterprise serves a public purpose. *See* Annotation, *Validity, Construction and Effect of Statutes Providing for Urban Redevelopment by Private Enterprise*, 44 A.L.R.2D 1414, 1420 (1955).

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II. PENALTY PROVISIONS IMPOSED BY STATUTE UPHELD

The South Carolina Court of Appeals held that a penalty provision imposed by statute for unjustifiable breach of contract was enforceable in *South Carolina Department of Health & Environmental Control v. Kennedy*.[19] The court of appeals found that the legislature has the authority to provide for such penalties for civil wrongs, irrespective of actual damages sustained. The court's conclusion is consistent with the general rule of giving deference to legislative intent when construing penalty provisions imposed by statute.

The South Carolina Department of Health and Environmental Control (DHEC) is authorized to enter into contracts[20] to provide loans to medical students. These loans are conditioned upon an agreement with the student that he will practice general medicine in a specified service area[21] within the state for a maximum period of up to three years. Completion of the service requirement constitutes full repayment of the loan.[22] The statute provides for imposition of a penalty of three times the amount of the entire benefits received, plus interest, if the student does not practice medicine according to the contract and if DHEC determines that the breach was unjustified.[23]

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19. 289 S.C. 73, 344 S.E.2d 859 (Ct. App. 1986).

20. "Before being granted a loan each applicant shall enter into a contract with the Department [DHEC], which is considered a contract with the State of South Carolina agreeing to the terms and conditions upon which the loan is granted to him." S.C. CODE ANN. § 59-111-540 (Law. Co-op. Supp. 1986). Section 59-111-510 provides: "The Department of Health and Environmental Control, hereinafter referred to as 'the Department', shall aid, assist, promote, and administer a fund known as 'The South Carolina Medical and Dental Loan Fund' with sums as may be appropriated by the General Assembly." S.C. CODE ANN. § 59-111-510 (Law. Co-op. Supp. 1986).

21. Lists of medical service areas are to be prepared annually by DHEC and are defined as areas within the state which have ratios of not more than one doctor for each two thousand people and a minimum population of two thousand. S.C. CODE ANN. § 59-111-530 (Law. Co-op. Supp. 1986).

22. "If the applicant receives a loan for four years he is only required to practice in the service area for three years, at the end of which time the loan is considered paid in full." S.C. CODE ANN. § 59-111-530 (Law. Co-op. Supp. 1986).

23. The statute reads in pertinent part:

> If the recipient of a loan fails without justifiable cause to practice medicine or dentistry in accordance with the terms of his contract, a penalty for failure to complete the contract must be imposed by the department. . . . However,

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Over a four year period, Kennedy received $24,000 from DHEC for his medical education. In accordance with section 59-111-530, this loan was conditioned upon his fulfillment of a three year service requirement in an approved medical service area. After completing his residency[24] he informed DHEC of his intent to practice internal medicine in Columbia, South Carolina. DHEC found that Kennedy violated his contract because he failed to meet the service requirement, and DHEC sued to recover the penalty.[25] The lower court, upon motion by both parties for summary judgment, held the repayment provision to be an unenforceable penalty constituting involuntary servitude and entered judgment against Kennedy for only the amount of the funds received ($24,000). The trial court did not address the constitutionality of the statute itself. The court of appeals reversed and remanded.

In upholding the penalty provision, the court of appeals relied on the principle that equity will not mitigate a penalty or forfeiture imposed by a statute since to do so would contravene the legislative intent.[26] The court noted that private parties to a contract may stipulate in advance an amount to be paid upon breach as liquidated damages,[27] but a provision for payment of a sum as punishment for default is a penalty and is invalid and unenforceable.[28] The court in *Kennedy* concluded, though, that the penalty was authorized by statute and was therefore not controlled by rules applicable to contracts between private par-

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where the Department determines that there is justifiable cause for the failure to practice pursuant to the terms of the contract, it may relieve the recipient of the obligation to practice according to the terms of the contract . . . .

S.C. CODE ANN. § 59-111-560 (Law. Co-op. Supp. 1986).

24. DHEC deferred Kennedy's service requirement during his residency period pursuant to S.C. CODE ANN. § 59-111-530 (Law. Co-op. Supp. 1986).

25. The South Carolina Department of the Attorney General is authorized to institute proceedings to recover amounts due the state upon breach of the contract. S.C. CODE ANN. § 59-111-560 (Law. Co-op. Supp. 1986).

26. 289 S.C. at 75-76, 344 S.E.2d at 861.

27. A liquidated damages provision is valid where (1) the damages reasonably anticipated to result from a breach are difficult to ascertain because of indefiniteness or uncertainty, and (2) the amount stipulated is either a reasonable estimate of damages that may probably be caused or reasonably proportionate to actual damages caused by the breach. Annotation, *Contractual Provision for Per Diem Payments for Delay in Performance as One for Liquidated Damages or Penalty*, 12 A.L.R.4TH 891, 899-900 (1982). *See generally* 22 AM. JUR. 2D *Damages* §§ 212-23 (1965).

28. Annot., *supra* note 27, at 899.

ties.[29] In so holding, the court recognized the authority of the legislature to provide civil penalties for violations of legally promulgated rules.

Kennedy is analogous to cases that have arisen in the context of recovery for the breach of public bonds.[30] As a general rule, the intent of the public body whose statute or ordinance requires the bond is an important element in determining whether the sum stipulated by the bond is to be construed as a penalty or as liquidated damages. This construction will in turn determine the extent of allowable recovery. In the absence of express or implied provisions to the contrary in the authorizing statute or ordinance, the full penalty is recoverable for the breach of the bond.[31]

A frequently cited case concerning recovery on a bond, cited also by the court of appeals in *Kennedy*, is *Clark v. Barnard*.[32] In upholding the enforceability of a performance bond required by Rhode Island for the construction of a railroad, the United States Supreme Court reasoned that the state "had perfect right to act upon its own policy and prescribe its own terms, as conditions of powers and privileges sought from its authority."[33] The Court reached this result although no actual damages were sustained by the state as a result of the breach of the bond conditions. Other courts have held, however, that only actual damages are recoverable on a bond. The courts that refuse to award more than actual damages have not based their holdings on the theory that the breach was a violation of a statutory duty.[34]

In *United States v. Swanson*[35] a federal court reached a result similar to that in *Kennedy*, but for a different reason. The

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29. *See* Salem v. Anson, 40 Or. 339, 67 P. 190 (1902).

30. *See generally* Annotation, *Entire Penalty as Recoverable for Breach of Bond Given to Public as Condition of License or Other Privilege, or Conditioned on Compliance with Law*, 103 A.L.R. 405 (1936).

31. *See* O'Kane v. Lederer, 4 F.2d 418 (E.D. Pa. 1923).

32. 108 U.S. 436 (1883).

33. *Id.* at 461.

34. *See* City of Summit v. Morris County Traction Co., 85 N.J.L. 193, 88 A. 1048 (1913). This case was distinguished from *Clark* because the bond in *Morris* was conditioned on the breach of any one or more of several covenants as opposed to only one. The *Morris* court, however, failed to recognize the statutory authority to provide for such penalties; *see also* Mayor of Brunswick v. Aetna Indem. Co., 4 Ga. App. 722, 62 S.E. 475 (1908).

35. 618 F. Supp. 1231 (E.D. Mich. 1985).

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court considered the validity of an analogous repayment requirement imposed by the National Health Corps Scholarship Program upon a student borrower's failure to comply with a medical service obligation.[36] The *Swanson* court viewed this provision as one for a liquidated damages sum rather than a penalty.[37] The court implied, however, that if the amount of damages had not been reasonable as liquidated damages, the repayment provision could have been unenforceable as a penalty.[38]

In relying on the authority of the legislature to impose civil penalties, the court of appeals recognized the legislative policy of providing health care to areas in need of assistance. This policy is clearly a proper legislative goal and the *Kennedy* court found that the legislature is authorized to choose the means by which to implement the policy. Further, in light of the holding in *Swanson*, the court of appeals would have been justified in finding the repayment requirement enforceable as a liquidated provision. The validity of this penalty provision can clearly be upheld on either theory.[39]

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36. 42 U.S.C. § 254m(a) (1982) provides that each individual who has entered into a written contract shall provide service in the full time clinical practice of such individual's profession as a member of the Corps for the period of obligated service provided in such contract. 42 U.S.C. § 254o(b)(1) (1982) provides a formula by which damages are to be calculated for a recipient's failure to begin or complete his service obligation. This essentially provides for the repayment of three times the amount of funds received adjusted in proportion to the amount of the service obligation actually met by the recipient, plus interest.

37. The court wrote:

> To estimate the damages which would be suffered by the loss of the services of a trained osteopathic physician for a three year period in a medically underserved area is difficult, if not impossible, to accurately determine. The Court cannot say that damages which the government would be entitled to receive for Defendant's breach of the contract bears no relation to the actual damages suffered by the government, or that they were not a fair and reasonable attempt to fix just compensation in the event of breach.

618 F. Supp. at 1243-44. The counsel for DHEC made a similar argument in *Kennedy*. 289 S.C. at 75, 344 S.E.2d at 861 (Ct. App. 1986); Brief of Appellant at 10-15.

38. "[T]his court holds that the liquidated damage provision does not operate as a penalty and is valid and enforceable in a court of law." 618 F. Supp. at 1244.

39. The court of appeals summarily disposed of the lower court's finding that the provision constituted involuntary servitude. Because Kennedy voluntarily entered into the contract with full knowledge of its terms, he was bound to comply with them. Moreover, the penalty is one for damages rather than the forced servitude of a doctor. In addition, it is difficult to see how the payment of $74,000 would be coercive enough to result in forced servitude, since physicians' salaries are commonly greater than $50,000 annually. For a compelling analysis in support of this argument, see Brief of Appellant at 16-18; *see also* 289 S.C. at 76-77, 344 S.E.2d at 862.

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